SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934

No. 663

JOHN A. SNYDER, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

INDEX

	Original	Print
Proceedings before U. S. Board of Tax Appeals	1	1
Docket entries	1	1
Amended petition	4	2
Exhibit "A"—Notice of deficiency	21	15
Exhibits "B" and "C"—Summary statements by months of purchases and sales of U. G. I. stock	25	18
Answer to amended petition	29	21
Opinion, Arundell, M.	32	23
Decision	36	28
Petition for review	36	26
Assignments of error	40	29
Notice of filing petition for review	42	30
Statement of evidence	43	30
Order approving statement of evidence	46	33
Præcipe for transcript of record	47	33
Clerk's certificate ..... (omitted in printing)	48	
Proceedings in U. S. C. C. A., Third Circuit	49	34
Argument and submission ..... (omitted in printing)	49	
Opinion, Woolley, J.	50	34
Judgment	59	41
Petition for rehearing ..... (omitted in printing)	60	
Order denying petition for rehearing	71	42
Clerk's certificate ..... (omitted in printing)	72	
Order allowing certiorari	73	42

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., FEBRUARY 14, 1935.

—5973-C

[fol. 1]

BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 49721

JOHN A. SNYDER, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appearances: For Taxpayer: Harry A. Fellows, Esq., Henry M. Ward, Esq.
For Comm'r: R. W. Wilson, Esq., W. W. Kerr, Esq.

DOCKET ENTRIES

Aug 4, 1930.	Petition received and filed. Taxpayer notified. (Fee paid.)
Aug. 5, 1930.	Copy of petition served on General Counsel.
Sept. 12, 1930.	Answer filed by General Counsel.
Sept. 1[illegible], 1930.	Copy of answer served on taxpayer. General Calendar.
Mar. 15, 1932.	Hearing set May 5, 1932.
Apr. 26, 1932.	Motion for continuance filed by taxpayer. 4/27/32, granted to Fall 1932.
Sept. 13, 1932.	Hearing set Oct. 27, 1932.
Oct. 15, 1932.	Motion for 90 days continuance filed by taxpayer. 10/19/32, granted to 1/25/33.
[fol. 2] Oct. 15, 1932.	Notice of appearance of Henry M. Ward as counsel filed.
Jan. 18, 1933.	Motion for 60 days continuance filed by taxpayer. 1/19/33, granted to 3/27/33.
Mar. 22, 1933.	Motion for leave to file amended petition, amendment tendered, filed by taxpayer.
Mar. 23, 1933.	Motion for continuance to a date not prior to May 15, 1933, filed by General Counsel.
Mar. 24, 1933.	Copy of motion and amended petition served on General Counsel.
Mar. 27, 1933.	Hearing had before Mr. Marquette on merits. Petitioner moves to amend petition—granted. Leave to amend answer granted. Continued to May 22, 1933.

Mar. 27, 1933. Order that amended petition lodged on March 22, 1933, be filed and respondent be given the usual time to answer and to continue proceedings for hearing on the merits to May 22, 1933, entered.

Apr. 24, 1933. Answer to amended petition filed by General Counsel. 4/28/33, copy served.

May 22, 1933. Hearing had before Mr. Arundell on merits. Submitted. Briefs due 6/30/33.

May 31, 1933. Transcript of hearing of May 22, 1933, filed.

[fol. 3] June 27, 1933. Motion for extension of 30 days from June 30, 1933 to file briefs filed by taxpayer. 6/27/33, granted.

July 29, 1933. Brief filed by taxpayer.

Sept. 14, 1933. Opinion rendered, C. Rogers Arundell, Div. 7. Decision will be entered for the respondent.

Sept. 16, 1933. Decision entered, Eugene Black, Div. 15.

Dec. 1, 1933. Supersedeas bond in the amount of $78,000. Approved and ordered filed.

Dec. 5, 1933. Petition for review by U. S. Circuit Court of Appeals (3) with assignments of error filed by taxpayer.

Dec. 5, 1933. Proof of service filed.

Dec. 13, 1933. Agreed statement of evidence lodged.

Dec. 13, 1933. Agreed statement of evidence approved and ordered filed.

Dec. 20, 1933. Præcipe with proof of service thereon filed by taxpayer.

[fol. 4] BEFORE UNITED STATES BOARD OF TAX APPEALS

[Title omitted]

AMENDED PETITION—Filed March 27, 1933

The above-named taxpayer hereby petitions for a redetermination of the deficiency determined by the Commissioner of Internal Revenue as set forth in his deficiency

letter dated June 6, 1930 (IT:AR:B-6:JMF-60D) and as a basis for this proceeding sets forth the following:

I. The petitioner is an individual residing and doing business in Philadelphia, Pennsylvania.

II. The said notice of deficiency, a copy of which is attached and marked Exhibit "A," was mailed to the petitioner on June 6, 1930 and within sixty days thereafter and on August 4, 1930 the petitioner filed his petition for redetermination with the Board of Tax Appeals.

III. The taxes in controversy are personal income taxes for the calendar year 1928 in the amount of $38,961.22.

[fol. 5] IV. The petitioner submits that the determination of the Commissioner is erroneous in the following respects:

(a) The Commissioner increased petitioner's taxable income for the year 1928 in the amount of $192,143.25, claimed to represent profits from the sale of stock certificates.

(b) The sole basis for increasing petitioner's taxable income in the amount stated was the application by the Commissioner of Article 58 Regulations 74, which provides as follows:

"When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots can not be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain. * * * "

(c) The said regulation is inapplicable to the transactions in the purchase and sale of shares of stock by brokers for account of petitioner during the year 1928 as more fully set forth herein.

(d) If applicable to such purchases and sales as herein set forth, petitioner submits that the said Article 58 above quoted was beyond the power of the Commissioner, was not authorized by law, and was in violation of rights secured to petitioner by the Constitution of the United States and particularly by the first clause of the First Section of the First Article, and by the Fifth Amendment, in that in mak-

ing such regulation the Commissioner attempted to exercise legislative power which by the First Section of the First Article of the Constitution is vested in the Congress of the United States and in that application of said article of said regulation deprives petitioner of his property without due process of law in violation of the provisions of the Fifth Amendment of the Constitution.

[fol. 6] V. The facts upon which petitioner relies in support of his petition are as follows:

In the years immediately preceding the calendar year 1928, and particularly in the years 1925, 1926, and 1927 petitioner, in addition to his regular employment as secretary of an insurance company on salary, was engaged in a business regularly carried on for profit, and in certain transactions entered into for profit, which business and transactions were the purchase and sale of shares of stock listed on the New York and Philadelphia Stock Exchange, carried on by the petitioner through stock brokers who were members of said stock exchanges. The said business and transactions had been carried on continuously by petitioner during the said prior years particularly in 1925, 1926 and 1927. During the period prior to 1928 (with one small exception which does not affect the questions involved) petitioner's operations in the stock market were confined to the purchase and sale of shares of the capital stock of only one corporation, namely United Gas Improvement Company, a public utility engaged in business and operating in the City of Philadelphia, Pennsylvania, and elsewhere. The said corporation is herein referred to for brevity as "U. G. I." the name by which it is commonly known in stock exchange transactions. Said corporation had a large share capital and its shares were among the most active and most largely dealt in in said stock exchanges.

VI. During the period prior to and throughout the year 1928 petitioner traded in said U. G. I. stock exclusively through margin accounts with stock brokers, and from time to time during said period increased his holdings of such stock solely through the process known as "pyramiding" as more fully hereinafter described. At the end of the year 1927 the petitioner had two margin accounts [fol. 7] with stock brokers; one with the firm of C. Clothier

Jones & Company, of 1603 Walnut Street, Philadelphia, and the other with MacDonald & Company, 234 Real Estate Trust Building, Philadelphia, Pennsylvania. Both of said accounts were margin accounts and all the shares of stock of U. G. I. bought by each of said brokers had been bought for account of petitioner through the process of "pyramiding" on a rising market. On the first day of January, 1928, said firm of Clothier Jones & Company held for account of petitioner as the result of the prior transactions to and including December 31, 1927, 2300 shares of U. G. I. stock against which there was a debit balance against petitioner on the books of said firm of $218,696.95. On the first day of January, 1928, said firm of MacDonald & Company, held for account of petitioner, as the result of the prior transactions to and including December 31, 1927, 3000 shares of U. G. I. stock against which there was a debit balance against petitioner on the books of said firm of $283,168.64.

VII. During the year 1928, from the 1st of January to the 31st of December, inclusive, the petitioner continued his operations in the stock market in U. G. I. stock through the said two brokers, both of whom were members of the New York and Philadelphia Stock Exchanges and carrying on their business in accordance with the established practice, rules and regulations of said Stock Exchanges. From time to time during the year 1928 the petitioner instructed said firm of Clothier Jones & Company to purchase and carry for his account and risk additional shares of said U. G. I. stock and to sell for his account certain shares of said stock. The total number of shares of said U. G. I. stock so sold by said brokers for account of the petitioner in 1928 was 3700, making an excess of U. G. I. stock purchased and held by said firm of Clothier Jones & Company [fol. 8] for account of the petitioner over the shares sold of 1200 shares, so that the number of U. G. I. shares carried by said brokers for account of the petitioner had increased in 1928 from 2300 to 3500 and the debit balance on the books of said firm of Clothier Jones & Company had increased from $218,696.95 on January 1, 1928, to $407,294.70 on December 31, 1928. The said balances on said dates and the intermediate balances on the first day of each month as reported to the petitioner by said brokers were in accordance with the customary course and practice of

business on the Stock Exchanges of New York and Philadelphia, reached by debiting petitioner with the purchase price of the U. G. I. stock purchased for his account on his orders together with all commissions, taxes, interest, and other debit items and by crediting his account from time to time with all proceeds of sale and with all dividends received by said brokers upon certain of the shares of stock carried by them for account of the petitioner.

VIII. From time to time during the year 1928 the petitioner instructed said firm of MacDonald & Company to purchase for his account and risk additional shares of said U. G. I. stock and to sell for his account certain shares of said stock. The total number of shares so purchased by said firm of MacDonald & Company during the year 1928 on petitioner's orders was 5700 and the total number of shares of U. G. I. stock so sold by said brokers for account of petitioner was 4200, making an excess of U. G. I. shares held by said firm of MacDonald & Company for account of petitioner over the shares sold of 1500 shares, so that the number of U. G. I. shares carried by said brokers for account of the petitioner had increased in 1928 from 3000 to 4500 and the debit balance on the books of said firm of MacDonald & Company had increased from $283,169.64 on [fol. 9] January 1, 1928, to $525,527.97 on December 31, 1928. The said balances on said dates and the intermediate balances on the first day of each month as reported to the petitioner by said brokers were, in accordance with the customary course and practice of business on the Stock Exchanges of New York and Philadelphia, reached by debiting petitioner with the purchase price of the U. G. I. stock purchased for his account on his orders together with all commissions, taxes, interest, and other debit items and by crediting his account from time to time with all proceeds of sale and with all dividends received by said brokers upon certain of the shares of stock carried by them for account of the petitioner.

IX. With respect to the transactions in the purchase and sale of U. G. I. stock through said two brokerage houses petitioner throughout the year 1928 was attempting to and did take advantage of the fluctuations in the market quotations of said U. G. I. stock, with the intent and purpose of increasing the number of shares of U. G. I. stock carried for his account by said brokers. By selling from time

to time in 1928 a part of the additional purchases of said stock petitioner was taking advantage of the turns of the market, selling stock from time to time when the market quotations were higher or slightly lower than at the time of purchase in the year 1928 and buying back equivalent amounts of stock when the quotations were lower or slightly higher, but the market was still rising.

X. During the said period from time to time the said brokers in fulfillment of selling orders given them by petitioner sold more U. G. I. stock than they then had on hand as a result of the purchases made for petitioner's account in 1928, but in each of such instances petitioner had given orders to sell various amounts of such U. G. I. [fol. 10] stock at the quotations in force on the day of sale, with the intent and purpose of buying back equivalent or greater amounts of such stock shortly thereafter, whenever the market quotations were sufficiently low to show a profit or only a small loss on the transaction. This intention was carried out and as above set forth petitioner caused the said brokers to purchase for his account during the year 1928 many more shares than he instructed them to sell for his account. All of such purchases and sales were made by said brokers, under petitioner's instructions, in the carrying out of the said business and transactions entered into by petitioner through the said brokers for the purpose and in fulfillment of the petitioner's increasing his holdings of said U. G. I. stock in the said margin accounts through the said process of "pyramiding" and it was not petitioner's intention at any time to have the said brokers sell for his account any of the shares of stock purchased in prior years or to realize any profit with respect to the earlier purchases. Petitioner's intention in general throughout the year 1928 was to increase the holdings of U. G. I. stock carried for his account by said brokers to as great an extent as the margin of his account permitted. Throughout 1928 said brokers, in accordance with the established practice of stock brokers and their customers in the purchase and sale of stock certificates on margin accounts, required petitioner to maintain at all times a sufficient credit balance or margin. This margin was represented by the difference between the current market quotations of all the shares of U. G. I. held by said brokers for his account and the debit balance against petitioner, rep-

resented by the amount paid for stock purchased and other debit items. Throughout the year 1928, as in prior years, petitioner was required by said brokers to keep at all times a "margin" or credit balance so computed, of not less than [fol. 11] 30 per cent, so that his debit balance might not exceed at any time 70 per cent. of the total credit balance computed on the basis of the daily market quotations of said U. G. I. stock, multiplied by the number of shares carried by the brokers to the credit of petitioner's account. Whenever because of a fall in the market quotations, petitioner's debit balance was in excess of 70 per cent. of his credit balance so computed said brokers required petitioner either to put up more margin in the form of cash or securities or to increase his credit balance by selling a sufficient number of shares of U. G. I. In all such instances petitioner ordered his brokers to sell and they sold accordingly a sufficient number of shares to make good petitioner's margin. In such instances the lack of a sufficient credit balance had been brought about by the debit having been increased through the most recent purchases and through a fall in the market, and in all such cases it was the intention of petitioner in accordance with the usual and established course of trading on the Stock Exchange to sell the stock last acquired, the purchase of which followed by the fall in market quotations had impaired his margin.

XI. The well-established course of dealing on the Stock Exchanges in New York and Philadelphia in the purchase and sale of securities through stock brokers in accordance with which all the transactions herein set forth were carried on is and was in the year 1928, with respect to margin accounts, substantially as follows:

The person desiring to operate in the stock market known as the "customer" gives to the stock broker orders, oral or written, to buy or sell, as the case may be, a designated number of shares of a designated stock. If the transaction is a purchase or a "long" transaction on margin the customer advances or "puts up" with the broker such percentage of the cost of the stock as may be required for [fol. 12] "margin." In 1928 the customer's margin required was usually not less than 30 per cent. and not over 40 per cent. depending on the activity of the stock and the credit rating of the customer. In some cases a cus-

tomer was allowed as was petitioner to some extent to keep a margin of less than 30 per cent. in dealing in certain active stocks such as U. G. I. Where all the transactions, as in the case of the petitioner, are in lots of 100 shares or multiples of 100 shares and there are no "odd lot" transactions, the broker executes the order on the floor of the Stock Exchange by purchasing the number of shares ordered. Under the rules of the Stock Exchange, which are binding upon all stock brokerage houses, members thereof, delivery of the stock must be made to the broker who buys, from the broker who sells, not later than the following day. In all cases where a margin account is involved, that is to say where the stock is not to be bought outright fully paid for and put in the name of the customer on the books of the company, the delivery of the stock is always made in the form of what is known as a "street certificate." A "street certificate" is a certificate for 100 shares of a designated stock listed on the New York or Philadelphia Stock Exchange, standing on the books of the corporation in the name of a brokerage house, a member of either Exchange. This stock certificate, endorsed in blank by the brokerage house in whose name it stands and is delivered not later than the following day to the broker who has purchased it. "Street certificates" in this form pass from hand to hand among the brokerage houses with the same freedom as currency or bank notes and are not customarily put in the name of the broker to whom or of the broker by whom the delivery is made. By agreement between the customer and the broker, as long as the certificates are carried by the broker on margin for [fol. 13] account of the customer, the broker has the right, which is customarily exercised and was exercised by the said brokers through whom the petitioner carried on his operations, of pledging such "street certificates" with banks or trust companies as collateral security for loans. In the course of the brokerage business large brokerage houses such as the said firm of C. Clothier Jones & Company and MacDonald & Company, have thousands of customers and carry for accounts of their various customers on margin many thousands of "street certificates." These "street certificates," together with other securities (such as bonds also carried by brokers for account of their customers who are dealing in bonds) are pledged with banks

and trust companies for loans of amounts which are required to meet the payments from day to day required for the purchase of securities by the brokers for account of their various customers. Banks and trust companies are not permitted to and will not make loans to brokers in excessive amounts, so that the brokers are required to and do make loans from many different banks and trust companies in the aggregate amounts needed. As collateral for these various loans, which the case of such large brokerage houses as those mentioned herein run into many millions of dollars, the brokers mingle all the "street certificates" which they happen to be carrying in one particular stock, such as U. G. I., with other street certificates of other stocks and the identity of the "street certificates" so pledged for the account of any particular customer is completely lost. Consequently it has been at all times since long before the establishment of the regulation of the Commissioner above referred to and continuously thereafter, impossible to identify in any active stock which the broker is carrying for the account of more than a few customers any certificate purchased for the account of any particular customer.

[fol. 14] XII. With respect to sales of stock certificates by brokers, the usual course of procedure, which was followed with respect to petitioner's account and has been followed at all times since long prior to the making of the said regulation and continuously thereafter, is that when the broker is required to make delivery of the certificates sold, he takes whatever "street certificates" of the particular stock may be the most conveniently available, either from such lot of street certificates of the particular stock as the broker may have in his office, or out of street certificates so pledged with some bank or trust company, in that case either paying off part of the loan or substituting other collateral. Consequently, for example, when in the instant case either broker executed an order given him by petitioner for the sale of one hundred, or a multiple of a hundred, shares of the U. G. I. stock, the broker did not necessarily or usually sell any one or more of the particular street certificates purchased for account of the petitioner, but in most instances sold street certificates held for account of other customers.

XIII. Under the custom and usage of the brokerage business, as carried on by brokers, members of the New York or Philadelphia Stock Exchanges, and under the contractual relations existing between all customers of such brokers operating margin accounts (including petitioner and the brokers above specified), the customer did not, nor did the petitioner in any instance, when a purchase was made for his account upon his order, acquire title to any specified certificates. What he acquired when he gave his broker an order to buy stock was the right to demand from the broker at any time delivery of an equal number of shares of the particular stock so purchased, but he did not acquire the right to delivery nor would delivery be made to him by the broker until, with respect to the shares of [fol. 15] stock so to be delivered, he had paid to the broker in cash or securities a sufficient amount to represent the aliquot part of the debit balance on the books of the broker attributable to the shares of stock to be delivered. A customer had not the right to demand delivery of any certificates without such payment if such delivery would result in reducing his credit balance of long stock carried for his account below the amount required for margin as above stated.

XIV. Throughout the year 1928 petitioner did not — any time require either of said brokers to deliver any stock to him nor did the petitioner at any time during the year 1928 make any further payments to either of said brokers either in cash or securities, but petitioner relied solely upon the "paper profit" which would have been realized at any time if the account had been closed and the shares of U. G. I. which the brokers were carrying for his account sold at current quotations and the proceeds of sale less the debit balance had been paid over to him. Throughout the year 1928 as the result of the operations of petitioner as herein above set forth these "paper profits" were sufficient, on a rising market, to enable the petitioner to accumulate during the year in his accounts with the respective brokers the numbers of shares above specified, and all of the transactions in the year 1928 with the said two brokers in the purchase and sale of U. G. I. stock were made for the purpose and had the effect of strengthening petitioner's position in the stock market, increasing his margin of "paper profit" and thereby enabling him to increase his holdings

and occupy the position which is commonly known as being "long" on the stock market.

XV. Under the rules and practice of the said stock exchanges the brokers were required to and did in each in-
[fol. 16] stance of a purchase or sale as the case might be for account of petitioner and for account of any and all other customers, deliver to petitioner, by mail or otherwise, on the day of purchase or sale, a memorandum of such purchase or sale stating the number of shares bought or sold, the name of the stock, and the name of the brokerage house from whom the stock was bought or to whom the stock was sold, as the case might be. The name of the broker from whom the stock was purchased did not necessarily, although it might, represent the broker in whose name the street certificate or certificates bought, stood on the books of the company and by whom the street certificate or certificates were endorsed. Neither of the said brokers at any time throughout the year 1928 caused any of the street certificates bought for account of petitioner to be put in his name on the books of United Gas Improvement Company nor did they customarily do so with respect to the thousands of other customers for whom they were carrying margin accounts. With respect to the U. G. I. stock sold none of the sales was made of any stock standing in the name of the petitioner but all such sales were made of street certificates, either those which happened to be in the office of the broker by whom the sale was made or those which might be taken out of securities pledged with banks or trust companies as above stated.

XVI. In making the purchases for petitioner's account and for account of the thousands of other customers which the said brokers were carrying on margin the transactions with respect to paying for the stock were substantially as follows:

The loans made by the respective banks and trust companies were on the basis of approximately 50 per cent. of the current market quotations of all the securities pledged
[fol. 17] as collateral for the various loans, so that, as market quotations rose the amount of loans could be increased, but as the market quotations fell, the amount of loans had to be curtailed or additional securities pledged. The cash supplied by petitioner to brokers together with the paper

profits as above described represented from 30 to 40 per cent. of the current daily quotations. The balance, namely, from 10 to 20 per cent., was supplied from the broker's working capital. This basis of transacting business was universally adopted with respect to all stocks listed on the New York and Philadelphia Stock Exchanges by all brokerage houses members of either or both of such exchanges. With respect to all margin accounts it had been adopted and was well recognized many years before the said regulation of the Commissioner was put into effect and was continuously in operation thereafter.

XVII. Petitioner submits as a particular ground for attacking the validity of the said regulation of the Commissioner, that it assumes a non-existent fact, namely, that there is any way in which in the case of any active margin account in an active stock such as U. G. I. it is possible to establish the identity of any certificate purchased or sold as the case may be, by a broker for account of his customer. Petitioner submits that the effect of this regulation, as applied to the facts in this case, is to make it impossible for petitioner to prove, as the fact is, that it was not his intention to sell at any time in the year 1928 any of the stock acquired in prior years which showed a large profit, and that it was not his intention at that time to realize any such large profit, but in the course of the transactions above described his intention was, and the effect of his acts was merely to strengthen his position in the market, and by realizing profits on the particular transaction of the year 1928 to increase his margin account and thereby [fol. 18] to enable his brokers to purchase for his account in the manner and on the basis above described, the additional shares of U. G. I. as above stated.

XVIII. Petitioner submits, therefore, that with respect to petitioner's transactions herein set forth the said regulation is wholly arbitrary and has no reasonable basis or justification, but was devised by the Commissioner of Internal Revenue during a rising market with the purpose and intent of increasing the amount of income tax chargeable against petitioner and other taxpayers similarly situated to as great an extent as was practicable, and thereby without warrant of law to penalize them by the imposition of arbitrary and oppressive taxes in connection with their

lawful purchases and sales of stock on margin accounts in accordance with the established practice of the Stock Exchanges of New York and Philadelphia and of other stock exchanges. Petitioner further submits that if the Commissioner has power to make this particular regulation with respect to a rising market, he has equally the power to make the opposite regulation with respect to a falling market and thereby to prevent the petitioner and others similarly dealing in stocks on margin accounts from deducting losses actually suffered by reason of their intent and purpose to sell the stock which show the largest losses.

XIX. It was the intent and purpose of petitioner and of the said brokers through whom he was operating in every instance, either to sell the last acquired stock first or to sell one or more hundred shares of stocks in the form of "street certificates" and shortly thereafter, when the market had fallen, to buy back an equivalent number with the purpose and intent of increasing petitioner's margin and thereby enabling him to have the said brokers acquire for [fol. 19] his account and to go "long" of additional shares of U. G. I. stock with the hope and expectation at such time in the future as the market might further rise, of selling all or a large part of his shares of U. G. I. stock at a great profit. There was no object, and it could not have been of any benefit or advantage to the petitioner to realize and convert into cash the paper profits which represented the great increase in the market quotations of U. G. I. stock from the time of purchase thereof in prior years to the time of the sale thereof in 1928. During the said period the market quotations of said stock were in many cases 100 or more points, that is to say 100 or more dollars per share, over and above the price at which they had been purchased in prior years. Under the course of trading adopted by petitioner no substantial profits could have been realized and drawn by the petitioner from his account with said brokers without impairing his margin and thereby making it impossible for him to accumulate in his account the additional shares of U. G. I. stock.

XX. Attached hereto as a part of this petition and marked Exhibits B and C are summary statements by months of all the transactions in U. G. I. stock herein referred to in the year 1928 in the two margin accounts with

C. Clothier Jones & Co. and MacDonald & Co. respectively showing the number of shares "long" to petitioner's credit on January 1, 1928, and at the end of each month, the number of shares bought and sold with dates of purchase and sale respectively, the debit items resulting from the purchases, the credit items resulting from the sales, the balance to the debit of petitioner's account as a result of the respective purchases and sales and the debit balances on Januaary 1, 1928, and at the end of each month in that year.

Wherefore, petitioner prays that the board redetermine [fol. 20] petitioner's net taxable income for the year 1928 and redetermine petitioner's deficiency if any in respect of income tax for the said year in such amount as may be established by law or determine that there is no deficiency for said year.

John A. Snyder, Petitioner, by (Sgd.) Harry A. Fellows, Attorney, Union Trust Building, Washington, D. C. (Sgd.) Henry M. Ward, Counsel, Washington, D. C.

Duly sworn to by John A. Snyder. Jurat omitted in printing.

[fol. 21] EXHIBIT "A" TO AMENDED PETITION

Treasury Department, Washington

Office of Commissioner of Internal Revenue

Jun. 6, 1930.

Mr. John A. Snyder,
c/o W. H. MacDade, 607 Bankers Trust Building,
Philadelphia, Pennsylvania.

SIR:

You are advised that the determination of your tax liability for the year 1928 disclosed a deficiency of $38,961.22 as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned.

Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement will expedite the closing of your return(s) by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the enclosed agreement, or on the date assessment is [fol. 22] made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully, Robt. H. Lucas, Commissioner; by (Sgd.) David Burnet, Deputy Commissioner.

Enclosures: Statement, Form 882, Form 870.

Statement

IT:AR:B-6. JMF-60D.

Jun. 6, 1930.

In re Mr. John A. Snyder, c/o W. H. MacDade, 607 Bankers Trust Building, Philadelphia, Pennsylvania

Tax Liability

Year	Corrected tax liability	Tax previously assessed	Deficiency
1928	$38,961.22	None	$38,961.22

The report of the internal revenue agent in charge at Philadelphia, Pennsylvania, has been reviewed and approved by this office.

Income reported	$5,352.60
Statutory loss reported	(59,206.99)
Net loss reported	($53,854.39)

Add:

1. Sale of securities	$192,143.25	
2. Statutory net loss reported	(59,206.99)	
Total increase		251,350.24
Ordinary net income adjusted		$197,495.85

[fol. 23] Explanation of Changes

1. The increase in profit from sale of stock is caused by using the method prescribed by article 58, Regulations 74 as follows:

"When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of lots cannot be determined, the stock shall be charged against the earliest purchase of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain * * *."

Inasmuch as the shares sold cannot be identified the profit must be computed as outlined above.

2. The net loss claimed from the year 1926 has been disallowed inasmuch as it was not shown conclusively that you were engaged in a business regularly carried on as defined in article 651, Regulations 74. The internal revenue agent has therefore been sustained in denying your protest.

Computation of Tax

Net income adjusted		$197,495.85
Less:		
Dividends	$33,363.55	
Personal Exemption	3,500.00	
		36,863.55
Balance subject to normal tax		$160,632.30
Normal tax at 1½% on $4,000.00		60.00
Normal tax at 3% on $4,000.00		120.00
Normal tax at 5% on $152,632.30		7,631.62
Surtax on $197,495.85		31,159.17
Total		$38,970.79

[fol. 24] Less:

Earned income credit	9.57
Tax Liability	$38,961.22
Previously assessed	None
Deficiency	$38,961.22

Payment should not be made until a bill is received from the collector of internal revenue for your district and remittance should then be made to him.

[fol. 25]

EXHIBIT "B" TO AMENDED PETITION

C. Clothier Jones & Company

Summary Statement by Months of Purchases and Sales of U. G. I. Stock, Dates, Numbers of Shares Bought and Sold, Prices and Debit Balances

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Jan.	1	2300							218,696.95
	31	2300							217,422.11
Feb.	6				200	113		2,2546	194,876.11
	9				200	112		2,2346	172,530.11
	29	1900							173,345.91
March	9		100	117			11,725		
	9		100	117			11,725		196,795.91
	12		100	118¾			11,900		208,695.91
	21		100	120			12,025		220,720.91
	31	2300							221,673.62
April	2		100	124			12,425		
	2		100	122			12,225		246,323.62
	10		100	126			12,625		258,948.62
	11		100	128			12,825		271,773.62
	16		100	131			13,125		
	16		100	134⅝			13,487.50		298,286.12
	30	2900							297,478.07
May	3		100	137			13,725		311,203.07
	7		100	146⅛			14,637.50		
	7		100	144			14,425		
	7		100	140			14,025		
	7		100	142¼			14,250		368,540.57
	8		100	148			14,825		383,365.57
	10				100	145		14,473	
	10				100	144⅝		14,435.50	
	10				100	144⅝		14,435.50	
	10				100	144½		14,423	
	10				100	144⅞		14,460.50	
	10				100	145		14,473	
	10				100	145		14,473	
	10				100	144⅞		14,460.50	
	10				100	145		14,473	
	10				100	145		14,473	238,785.57
	14		100	147¾			14,800		
	14		100	148¼			14,850		
	14		100	148½			14,850		
	14		100	148¼			14,850		

EXHIBIT "B" TO AMENDED PETITION—Continued

[fol. 26]

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
May	14		100	147¼			14,750		312,885.57
	18				100	142		14,173	
	18				100	142		14,173	284,539.57
	23				100	140		13,973	
	23				200	140¼		27,996	242,570.57
	31	2500							244,035.16
June	12				100	139		13,873	
	12				100	138		13,773	216,389.16
	13				100	132⅜		13,248	
	13				100	132⅛		13,223	
	13				100	136½		13,660.50	
	13				100	134¾		13,448	
	13				100	136		13,573	
	13				100	131¼		13,098	136,138.66
	14		100	133⅛			13,362.50		
	14		100	133⅛			13,362.50		
	14		100	135½			13,575		
	14		100	134½			13,475		189,913.66
	15		100	138½			13,850		
	15		100	137½			13,775		217,538.66
	15		100	138½			13,875		231,413.66
	18		100	139			13,925		245,338.66
	30	2500							246,721
July	31	2500							245,801.65
Aug.	31	2500							247,839.02
Sept.	29	2500							249,491.28
Oct.	8		500	140¾			70,500		319,991.28
	22				100	146⅛		14,585.50	
	22				100	146		14,573	
	22				100	146½		14,623	
	22				200	145½		29,046	244,663.78
	31	2500							248,528.14
Nov.	5		400	146½			58,700		
	5		100	146½			14,675		319,003.14
	16		100	161¾			16,200		
	16		100	161¾			16,200		
	16		100	161¾			16,200		
	16		100	161¾			16,200		
	16		100	161¾			16,200		403,403.14
	30	3500							405,642.94
Dec.	10				100	152⅛		15,185.50	
	10				100	152⅛		15,185.50	

[fol. 27]

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Dec.	10				100	152⅛		15,185.50	360,086.44
	11				100	151		15,073	
	11				100	152		15,173	329,840.44
	13		100	157¼			15,750		345,590.44
	26		100	159			15,925		
	26		100	162			16,225		
	26		100	160½			16,075		
	26		100	158			15,825		409,640.44
	31	3500							407,294.70

EXHIBIT "C" TO AMENDED PETITION

MacDonald & Company

Summary Statement by Months of Purchases and Sales of U. G. I. Stock, Dates, Numbers of Shares Bought and Sold, Prices and Debit Balances

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Jan.	1	3000							283,168.64
	16		100	116½			11,675		280,131.14
	31	3100							293,166.97
Feb.	6				200	113		22,546	270,620.97
	9				200	112		22,346	248,274.97
	29	2700							249,426.36
March	9		200	115⅞			23,225		272,651.36
	12		100	119¾			11,900		284,551.36
	12		100	120½			12,075		296,626.36
	31	3100							297,938.74
April	2		100	122½			12,275		
	2		100	124½			12,475		322,688.74
	10		100	126½			12,675		335,363.74
	11		100	128¾			12,900		349,263.74
	16		100	131			13,125		
	16		100	134			13,425		372,813.74
	30	3700							374,487.54
May	3		100	137			13,725		388,212.54
	7		100	140			14,025		
	7		100	142			14,225		
	7		100	144			14,425		
	7		100	146			14,625		445,512.54
	8		100	148			14,825		460,337.54

[fol. 28]

May	10				800	144¾			
	10				200	144⅝		144,267.50	316,070.04
	11				500	146		72,865	243,205.04
	14		300	147½					
	14		100	147⅝					
	14		100	147¼			73,837.50		317,042.54
	25		200	145½			29,150		346,192.54
	31	3500							347,968
June	12				100	139		13,873	334,095
	12				100	138		13,773	320,322
	13				100	136⅞		13,660.50	
	13				100	132½		13,223	
	13				100	132⅞		13,260.50	
	13				100	136		13,573	
	13				100	134¾		13,448	
	13				100	131½		13,123	240,034
	14		200	134⅝			26,975		
	14		100	135½			13,575		280,584
	15		100	137½			13,775		
	15		200	138¼			27,700		322,059
	18		100	139			13,925		
	18		100	138¾			13,900		349,884
	21				500	133		66,365	283,519
	29		200	135⅞			27,225		311,244
	30	3200							313,113.25
July	2		200	137			27,450		340,563.25
	5		100	138			13,825		354,350.75
	31	3500							353,152.96

EXHIBIT "C" TO AMENDED PETITION—Continued

1928		Long shares U. G. I.	Dr. Bought shares	at	Cr. Sold shares	at	Dr. Purchase price	Cr. Sales price	Dr. Balances
Aug.	31	3500							355,433:73
Sept.	14				800	142¾			
	14				100	143½			
	14				100	143⅞		142,667.50	212,766.23
	30	2500							215,013.78
Oct.	3		1000	141			141,250		356,263.78
	31	3500							356,041.50
Nov.	8		500	156½			78,375		434,416.50
	21		500	168			84,125		518,541.50
	30	4500							521,375.08
Dec.	31	4500							525,527.97

[fol. 29] BEFORE U. S. BOARD OF TAX APPEALS

ANSWER TO AMENDED PETITION—Filed April 24, 1933

Come now the Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, and for answer to the amended petition filed in the above-entitled appeal, admits and denies as follows:

I. Admits the allegations contained in paragraph I of the amended petition.

II. Admits the allegations contained in paragraph II of the amended petition.

III. Admits the allegations contained in paragraph III of the amended petition.

IV. Denies the allegations of error contained in subparagraphs (a) to (d), inclusive, of paragraph IV of the amended petition.

V. Admits the allegations contained in paragraph V of the amended petition, except that the respondent specifically denies that the petitioner was, during the year 1928, engaged in any trade or business other than that of Secretary of the Mechanics Insurance Company at Philadelphia, Pennsylvania, and further specifically denies that the brokerage accounts carred and maintained by the petitioner during said year constituted a trade or business within the meaning of any provision of the Revenue Act of 1928.

VI. Admits the allegations contained in paragraph VI of the amended petition.

[fol. 30] VII. Admits the allegations contained in paragraph VII of the amended petition.

VIII. Admits the allegations contained in paragraph VIII of the amended petition.

IX. Denies the allegations contained in paragraph IX of the amended petition.

X. Denies the allegations contained in paragraph X of the amended petition.

XI. Admits the allegations contained in paragraph XI of the amended petition.

XII. Admits the allegations contained in paragraph XII of the amended petition.

XIII. Admits the allegations contained in paragraph XIII of the amended petition.

XIV. Admits the allegations contained in paragraph XIV of the amended petition, except that the respondent specifically denies that the transactions between the petitioner and the stock brokers during the year 1928 in the purchase and sale of U. G. I. stock were made for the purpose of strengthening petitioner's position in the stock market, increasing his margin of "paper profit" and thereby enabling him to increase his holdings and occupy the position which is commonly known as being "long" on the stock market, as alleged in said paragraph XIV thereof.

XV. Admits the allegations contained in paragraph XV of the amended petition.

XVI. Admits the allegations contained in paragraph XVI of the amended petition.

[fol. 31] XVII. Denies the allegations contained in paragraph XVII of the amended petition.

XVIII. Denies the allegations contained in paragraph XVIII of the amended petition.

XIX. Denies the allegations contained in paragraph XIX of the amended petition.

XX. Admits the allegations contained in paragraph XX of the amended petition.

Denies generally each and every allegation contained in the amended petition not hereinbefore specifically admitted, qualified or denied.

Wherefore, it is prayed that petitioner's appeal be denied.

(Signed) C. M. Charest, General Counsel, Bureau of Internal Revenue. Of Counsel: R. W. Wilson, Special Attorney, Bureau of Internal Revenue.

[fol. 32] BEFORE UNITED STATES BOARD OF TAX APPEALS

Docket No. 49721

Promulgated September 14, 1933

JOHN A. SNYDER, Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Where petitioner bought and sold stock without identifying the particular lots, gain or loss on sales is to be computed on the basis of the cost of the earliest purchases. John A. Snyder, 20 B. T. A. 778; affd., 54 Fed. (2d) 57.

Henry M. Ward, Esq., and Harry A. Fellows, Esq., for the petitioner.

R. W. Wilson, Esq., and W. W. Kerr, Esq., for the respondent.

OPINION—Entered September 14, 1933

ARUNDELL:

The respondent's determination of a deficiency in income tax in the amount of $38,961.22 for the year 1928 arises out of his application of the rule of "first in, first out" to sales of stock made by Petitioner in the taxable year.

The facts upon which the case was submitted are those alleged in the amended petition and admitted in the re-

spondent's answer thereto, and those which it was stipulated the petitioner would testify to if present. For the [fol. 33] purposes of this report the pertinent facts may be briefly summarized.

In 1928 and several prior years petitioner dealt in stock of the United Gas Improvement Co. He traded through two brokerage houses on margin and pyramided his purchases. Upon a decline in the market so that his margin fell below the required percentage the brokers reduced his debit balance by sufficient sales to make up the deficiency in the margin. Upon a rise in the market the paper profits were used to increase his holdings of the stock. By this method of operation the stock standing to petitioner's credit on the brokers' books increased during the year from 5,300 shares to 8,000 shares, an increase of 2,700 shares. At the same time his debit cash balance on the brokers' books increased from $501,865.59 to $932,822.67, an increase of $430,957.08. These changes were the result of sales by the brokers at various dates throughout the year of a total of 7,900 shares and the purchase of 10,600 shares for petitioner's account. Purchases and sales affecting petitioner's account were entirely through the medium of street certificates handled by the brokers, who debited and credited petitioner's account to reflect the transactions, and at no time during the year did the brokers, on the one hand, or petitioner, on the other, deliver to each other actual stock certificate.

The substance of petitioner's testimony, offered by stipulation, was that in each case where a sale was made it was his intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount in order to increase his margin and acquire additional shares of the stock.

In determining the deficiency the respondent applied to petitioner's stock transaction the method of computation prescribed by article 58 of Regulations 74, as follows:

[fol. 34] When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots can not be determined, the stock sold shall be charged against the earliest purchases of such stock. The excess of the amount realized on the sale over the cost or other basis of the stock will constitute gain.

The applicability and validity of the above article of the regulations, commonly known as the rule of "first in, first out," are the only questions presented for decision. The same petitioner was before us in a proceeding reported at 20 B. T. A. 778, contesting a deficiency arising out of similar transactions in the same stock in the year 1925. In that case we sustained the respondent's application of the rule in controversy here, and on appeal by the petitioner our decision was affirmed by the Circuit Court of Appeals, Third Circuit, in an opinion reported at 54 Fed. (2d) 57. In the opinion of the Board it was said that there was no evidence of "petitioner's intention to sell any designated stock." Evidently to meet this situation petitioner's testimony was given in this case to the effect that in each sale he intended to sell the most recently acquired stock. This, however, does not establish that the sales were made in that order, and we are unable to find that they were so made in view of the stipulated facts that there were no deliveries of stock certificates, and the transactions were entirely through the medium of street certificates which were not identified or in any way earmarked for petitioner's account. Consequently, the facts upon which we have to go here are in no way different (save as to amounts) from those in the previous case.

Petitioner's principal argument is that the regulation applied here is invalid, under the decision in Heiner v. Donnan, 285 U. S. 312, which was decided since the previous case involving this same taxpayer. The Donnan case dealt [fol. 35] with a conclusive presumption; hence, it involved an entirely different question and is readily distinguishable from this case, in which the presumption is rebuttable. "A rebuttable presumption clearly is a rule of evidence" (Heiner v. Donnan, supra), and "casts upon the person against whom it is applied the duty of going forward with his evidence on the particular point to which the presumption relates." Manley v. Georgia, 279 U. S. 1. It does not estop the taxpayer from establishing the existence of a fact. Where the taxpayer identifies the stock traded in the presumption does not apply. Howbert v. Penrose, 38 Fed. (2d) 577; Cleveland Trust Co., Executor, 24 B. T. A. 132. The presumption announced in the regulations merely follows the rule that has been in effect at least since the decision in Towne v. McElligott (decided in 1921), 274

Fed. 960; hence, it cannot be said to work any hardship on the taxpayer, inasmuch as he had ample warning of the necessity of putting his accounts in shape to enable him to identify his purchases and sales.

Decision will be entered for the respondent.

[fol. 36] Before U. S. Board of Tax Appeals

Decision—Entered September 16, 1933

Pursuant to the Board's opinion promulgated September 14, 1933, it is

Ordered and decided, That there is a deficiency in income tax for the year 1928 in the amount of $38,961.22.

(Sgd.) Eugene Black, Member.

In United States Circuit Court of Appeals

Petition for Review of a Decision of the United States Board of Tax Appeals—Filed December 5, 1933

To the Honorable the Judges of the United States Circuit Court of Appeals for the Third Circuit:

Now comes John A. Snyder, petitioner, by his attorney and counsel and brings this his petition for review of the order of redetermination made by the United States Board of Tax Appeals September 14, 1933 (Docket No. 49721) and shows to the Court as follows:

I. Jurisdiction. The petitioner is a resident of Philadelphia, Pennsylvania, within the Third Judicial Circuit. The return was filed with the Collector of Internal Revenue at the city of Philadelphia.

II. Nature of Controversy. The question presented is one of law upon conceded facts, namely in what amount [fol. 37] petitioner is liable to a deficiency assessment of income tax for the year 1928 upon a profit claimed by the Commissioner to have been realized as a result of certain operations of purchase and sale of shares of stock in the stock market through and by means of margin accounts with stock brokers by the process commonly known as

"pyramiding." The petitioner claims that the net taxable income on which the tax should be computed is $6,308.55 and that the correct amount of the deficiency is $1,896.47. The Commissioner claims that the net income is $197,495.85 and that the tax liability is $38,961.22. The Board of Tax Appeals sustained the ruling of the Commissioner.

III. Record before the Board. The case was submitted to the Board of Tax Appeals upon an amended petition in which the facts were fully set forth, an answer which admitted all but a few of the facts alleged, and a statement of facts proving the facts at issue, received by stipulation in lieu of testimony. No oral evidence was offered by either party.

IV. Questions of Law Presented. The case involves:

First. The applicability to the petitioner's operations on the stock market, for the year 1928, which constituted a trade or business regularly carried on for profit, of the rule of "first in first out" (Article 58, Regulations 74) whereby the results of the transactions for the tax year are disregarded and transactions in prior years examined, in violation of the intent of Congress and rulings of the courts that the transactions of each tax year should be considered separately.

Second. If applicable, the power of the Commissioner in view of the terms of the statute to make and enforce this [fol. 38] rule with respect to petitioner's operations.

Third. If applicable, whether the regulations, as applied to and enforced against petitioner, is not void, under the authority of Heiner v. Donnan, 285 U. S. 312, in that an arbitrary and irrebutable presumption is thereby established which makes it impossible for petitioner to establish the facts by testimony and has the effect of a conclusive presumption.

V. Statement of Facts. On January 1, 1928, petitioner was "long" 5300 shares of United Gas Improvement Co. stock, known as "U. G. I.", which he had acquired in prior years. His debit cash balance on the broker's books was then $501,865.59. In 1928 the brokers sold on various dates 7,900 shares, and bought 10,600 shares, of U. G. I. Petitioner's debit balance was increased to $932,822.67, an increase of $430,957.08. All purchases and sales were made

for petitioner's account by his brokers in the form of street certificates. There was no delivery of certificates between the brokers and petitioner. The certificates of U. G. I. bought by the brokers for petitioner's account, were mingled with thousands of other street certificates of U. G. I. and other stocks and pledged by the brokers with various banks for loans. The petitioner did not at any time own any specified certificates and had no title to or ownership of any certificates. The brokers were under no obligation to hold for petitioner's account any of the certificates bought for his account, and, when they sold U. G. I. on petitioner's orders, they were free to and did deliver any available certificates for a like number of shares, out of lots held for any of their other customers. The petitioner had the right, on payment of an aliquot amount of his debit balance, to de- [fol. 39] mand delivery of so many shares of U. G. I., but the brokers could then deliver any conveniently available street certificates, whether originally purchased for the account of petitioner, or of any other customer. There was no way of identifying any of the certificates while held by the brokers, either those first acquired, those last acquired, or those acquired at any time. The brokerage business on the stock exchanges has always, with respect to margin accounts, been conducted on this basis, and, if the certificates purchased and sold on margin for the thousands of customers were specifically identified and allocated to particular customers the brokerage business could not be carried on. It was petitioner's intention throughout 1928 to accumulate as many additional shares of U. G. I. as market conditions might permit and he sold only when necessary, either because a fall in current daily quotations had impaired his margin, or because by realizing the "paper profit" on a quick turnover, he could improve his market position. In all instances it was his intention to sell the certificates, the purchase of which had brought about the occasion for the sale, in other words to sell the last acquired stock. It was not petitioner's intention at any time to realize in cash the large paper profits shown by comparison of the purchase price of certificates bought in prior years with the prices realized on sales in 1928, nor would it have been of any benefit to petitioner to make sales on the basis of realizing and withdrawing cash profits. Such profits could not have been withdrawn without impairment

of margin and the income tax applicable would have absorbed a large part of the profits.

[fol. 40] ASSIGNMENT OF ERRORS

The Board of Tax Appeals erred in the following particulars:

1. In holding that upon the facts Article 58, Regulations 74, was applicable to petitioner's trade or business of operating on the stock exchange.

2. In disregarding the result of petitioner's operations in this trade or business for the year 1928.

3. In holding that in computing income tax upon petitioner's operations in such trade or business for 1928 the price paid for shares of stock bought in prior years was controlling in determining whether a profit was realized or a loss sustained with respect to shares sold in 1928.

4. In holding that, in so far as applicable to the transactions here involved, the Commissioner was authorized by law to enforce said Article 58 of Regulations 74.

5. In holding that, if authorized by any Act of Congress, the enforcement of said Article 58 of Regulations 74 did not deprive the petitioner of his liberty and property in violation of the Fifth Amendment of the Constitution of the United States.

6. In holding that upon the conceded facts the determination of the Commissioner should be affirmed.

Wherefore petitioner prays that the order of redetermination of the Board of Tax Appeals be reversed and the tax recomputed in accordance with law and that the record [fol. 41] of proceedings be certified to the Circuit Court of Appeals for the Third Circuit.

Dated December 8, 1933.

Harry A. Fellows, Attorney for Petitioner, Union Trust Building, Washington, D. C. Henry M. Ward, of Counsel, 726 Jackson Place, Washington, D. C.

Duly sworn to by Harry A. Fellows. Jurat omitted in printing.

[fol. 42] In United States Circuit Court of Appeals

Notice of Filing Petition for Review

To E. Barrett Prettyman, Esq., General Counsel, Bureau of Internal Revenue, Washington, D. C.:

You are hereby notified that John A. Snyder, by his attorneys, Harry A. Fellows and Henry M. Ward did, on the fifth day of December, 1933, file with the Clerk of the United States Board of Tax Appeals, at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the Third Circuit, of the decision of the Board heretofore rendered in the above-entitled case. A copy of the petition for review and the assignments of error as filed is hereto attached and served upon you.

Dated this fifth day of December, 1933.

Harry A. Fellows, Henry M. Ward, Attorneys for Petitioner.

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this fifth day of December, 1933.

E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue.

[fol. 43] Before U. S. Board of Tax Appeals

Statement of Evidence—Filed December 13, 1933

The above-entitled cause came on for hearing May 22, 1933, before the Honorable C. Rogers Arundell, Member of the United States Board of Tax Appeals, at Washington, D. C., whereupon the following proceedings were had:

Counsel for the petitioner opened the case and stated that it would be submitted upon the amended petition, the answer and a statement of evidence to be received by stipulation. After this statement the following proceedings were had:

The Member: Are you going to have evidence of the fact that the certificates sold were not the earlier purchases or

are you going to argue that the presumption of the Commissioner is not proper and you are going to indulge in a presumption of your own?

Mr. Ward (counsel for petitioner): No. We offer in evidence this statement here with regard to the intention of the taxpayer, and I might read it to your Honor, as this relates to the only allegations of the amended petition which are denied. All of the other allegations are admitted.

The Member: Is this a matter of stipulation between the parties?

Mr. Wilson (counsel for respondent): To the extent that the statement which counsel has prepared and which he is about to offer in evidence represents the testimony which the petitioner would give if he were present, it is admitted that would be his testimony.

The Member: So you are stipulating that. You are not stipulating it is true, but that if present the petitioner would testify to that.

Mr. Wilson: Yes.

[fol. 44] Mr. Ward: That is correct.

Mr. Wilson: The government reserves all objections, of course.

The Member: Has that been signed?

Mr. Wilson: No, your Honor.

Mr. Ward: Shall I read it, your Honor?

The Member: All right.

Mr. Ward: It is agreed that in view of the inability of the petitioner-taxpayer because of illness to attend on the hearing in this case, it is stipulated between the parties that if said John A. Snyder were called as a witness in behalf of petitioner he would testify as follows with respect to the allegations in the amended petition which are denied by the respondent.

Paragraph X. It was the intention of the petitioner throughout the year 1928 to increase his holdings of shares of the United Gas Improvement Company stock in his margin accounts with the stock brokers. In each instance of sale of stock, on the dates and in the amounts specified in the schedules attached to the amended petition and marked, respectively, Exhibits B and C, the respective stock brokers required the petitioner, because of a fall in the market quotations of said U. G. I. stock, either to put up more margin in the form of cash or securities, or to increase

his credit balance by selling a sufficient number of shares of the said stock. In each of such instances petitioner ordered said brokers to sell the various amounts of such stock mentioned in said Exhibits B and C, at the quotations in force on the day of sale, and in each instance petitioner had the intent and purpose of buying back equal or greater amounts of said stock shortly thereafter, according to the market quotations. It was not at any time the petitioner's intention to sell any of the shares of stock purchased in prior years which showed a large paper profit but it was [fol. 45] his intention in each instance of sale on the dates and in the amounts specified in said Exhibits B and C to sell the last acquired stock, the purchase of which followed by the subsequent market fluctuations had brought about an impairment of his margin below the 30 per cent. margin which the brokers required him to maintain. Throughout the year whenever petitioner's cash debit in his account with each of the said brokers was in excess of 70 per cent. of the daily market quotations of the total shares to his credit, he made such sales in accordance with the requirements of the said respective brokers. In all such instances the lack of sufficient margin had been brought about by the debit having been increased through the more recent purchases and through the fall in the market quotations of said stock.

Paragraph XIV. All the transactions in the year 1928 of said brokers in the purchase and sale of U. G. I stock which had the effect of strengthening petitioner's position in the stock market, were made for that purpose and for the purpose of increasing his margin of "paper profit" and thereby enabling him to increase his holdings and occupy the position commonly known as "long" on the stock market.

Paragraph XIX. With respect to each of the items of sale of shares of stock specified in Exhibits B and C it was petitioner's intention to sell the last acquired stock first and shortly thereafter to buy back an equivalent amount, in order to increase his margin and to enable him through purchases made by said brokers to go "long" of additional shares of said stock, with the hope and expectation, on a further rise in the market, of selling all or a large part of his shares of said stock at a great profit. Throughout 1928 the petitioner did not intend to make any large profits

computed by reference to the purchase price of the shares of said stock acquired in prior years and the sale price of an equal number of shares in 1928 nor, if such profits had [fol. 46] been made, could they have been withdrawn in cash without impairing petitioner's margin and thereby necessitating the sale of additional shares.

The respondent will, upon the hearing, raise such objections to any and all of the above testimony as may seem to him advisable.

The Member: If he had drawn out nothing, what then?

Mr. Ward: He would have had to sell the stock or else put up more margin.

The Member: Is this the completed case; is it submitted now; you have no testimony to put in?

Mr. Wilson: No, sir.

Mr. Ward: Nothing further.

The Member: We will close the record on the testimony.

No other evidence was offered by either party and the case was submitted to the Board on a brief filed by the petitioner.

The foregoing statement of evidence is hereby approved and it is stipulated that the same may be examined and approved by the proper member of the Board of Tax Appeals without notice.

December 7, 1933.

Harry A. Fellows, Attorney for Petitioner; Henry M. Ward, of Counsel. E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue.

The foregoing statement of evidence examined and approved this thirteenth day of December, 1933.

(Sgd.) C. Rogers Arundell, Member, Board of Tax Appeals.

[fol. 47] Before U. S. Board of Tax Appeals

Præcipe for Transcript of Record—Filed December 20, 1933

To the Clerk of the Board of Tax Appeals:

Sir:

You are requested to make a transcript of the record to be filed in the United States Circuit Court of Appeals for

the Third Circuit at Philadelphia, Pennsylvania, pursuant to the petition for review filed herein and to include in such transcript copies of the following documents, duly certified as correct:

1. Docket entries of proceedings before the Board.
2. Amended petition, filed March 22, 1933.
3. Answer to amended petition, filed April 24, 1933.
4. Statement of evidence as settled.
5. Opinion of the Board filed September 14, 1933.
6. Order of redetermination filed September 14, 1933.
7. Petition for review with proof of service.
8. This præcipe.

Respectfully, Harry A. Fellows, Attorney for Petitioner; Henry M. Ward, of Counsel.

We acknowledge service of the foregoing præcipe this twentieth day of December, 1933.

E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue.

[fol. 48] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 49] Minute entry of argument and submission, May 2, 1934, omitted in printing.

[fol. 50] In United States Circuit Court of Appeals for the Third Circuit

March Term, 1934

No. 5419

John A. Snyder, Petitioner,

v.

Commissioner of Internal Revenue, Respondent

On Petition for Review from the United States Board of Tax Appeals

Before Woolley, Davis and Thompson, Circuit Judges

Opinion—Filed September 18, 1934

Woolley, Circuit Judge:

The Commissioner of Internal Revenue found a deficiency tax against Snyder arising out of marginal transac-

tions in the year 1928 which were similar in character to marginal transactions of the same taxpayer in 1925 on which this court passed in Snyder v. Commissioner, 54 Fed. (2d) 57. The Commissioner claims the decision in that case is res judicata of the matter raised on the present petition. Although the law may be the same, the facts, though similar, are different and, being different, they were not passed upon in that case. We hold against the Commissioner's contention of res judicata.

From the deficiency tax assessed by the Commissioner in the instant case, reckoned by setting off the last sales of [fol. 51] shares of stock against shares earliest purchased, Snyder appealed to the United States Board of Tax Appeals. That tribunal discussed in its opinion two questions: one, the validity of Article 58 of Regulations 74 promulgated under the Revenue Act of 1928; the other, the applicability of the regulation to the facts of this case. Snyder is here on petition to review the Board's order sustaining the tax assessed by the Commissioner.

The regulation whose validity is challenged is in these words:

"When shares of stock in a corporation are sold from lots purchased at different dates and at different prices and the identity of the lots can not be determined, the stocks sold shall be charged against the earliest purchases of such stock. * * * "

The validity of this regulation, and of like ones under previous statutes, now, for brevity, called the "First in, first out" rule, has repeatedly been sustained by this court and other courts. Snyder v. Commissioner, 54 Fed. (2d) 57; Commissioner v. Merchants and Manufacturers Fire Insurance Company, — Fed. (2d) —; Skinner v. Eaton, Collector, 45 Fed. (2d) 568; Howbert v. Penrose, 38 Fed. (2d) 577, 579.

The usual ground of attack has been that the rule is arbitrary and capricious and therefore in contravention of the due process clause of the Fifth Amendment to the Constitution. This court has held that while the rule is, from the very nature of the situations to which it applies, fixed and peremptory and in that sense arbitrary, it is, from the latitude of its words, not inflexible or capricious and therefore is not unreasonable. Since this pronouncement,

Heiner v. Donnan, 285 U. S. 312, has been decided. On that case the petitioner here takes a new stand. By that decision the Supreme Court held that Section 302 (c) of the Revenue Act of 1926, creating a presumption that gifts [fol. 52] made within two years of the donor's death were made in contemplation of death, was unconstitutional. The petitioner says that the rule which, on failure to identify shares sold, affords a presumption that the shares sold were those first bought is likewise unconstitutional. There is really no analogy between the provision of the statute under consideration by the Supreme Court in the Heiner case and the terms of the rule here under discussion. There the presumption was "conclusive" and made so by the statute. Here the presumption is rebuttable, hence constitutional. Cockrill v. California, 268 U. S. 258, 261; Yee Hem v. United States, 268 U. S. 178, 183-184; Mobile, J. & K. C. R. R. v. Turnipseed, 219 U. S. 35, 42-43. The taxpayer is given every opportunity to identify the shares he has sold and to prove his loss or gain accordingly. Indeed, the rule comes into operation only "when" the identity of the shares sold cannot be determined, which usually happens when the owner in ordering their sale has failed to identify the lots in which they were purchased. In such case there must be some way of determining for the benefit of the taxpayer his losses or gains in his taxable transactions and, similarly, of determining what taxes the government is entitled to exact. Except for this rule or some similar rule, efficiently to administer the revenue act, a vast multitude of potential taxpayers dealing in the purchase and sale of shares on margin and actually making profits would escape taxation because of their inability or disinclination to identify the shares sold and the government would lose the taxes which the statute imposes.

We re-state our judgment that the rule is valid.

The petitioner next contends that the rule, if valid, is not applicable to the instant case because it is inconsistent with the Revenue Act of 1928 which provides (Sections 11, 12, 21, 22 and 23) that there shall be levied, collected and [fol. 53] paid "for each taxable year" normal and surtaxes at certain rates. The substance of this contention is that the annual tax is to be levied and paid only on transactions begun and completed within the "taxable year" and to that end the entire series of the petitioner's marginal transac-

tions in 1928 (the tax year) should be segregated from all transactions in prior years and that transactions of sale in the tax year should be charged only against transactions of purchase in that year, leaving open and unanswered the question how profits from later sales of shares purchased earlier can be taxed. The infirmity in this contention lies in the fact that a transaction of sale of shares previously purchased, yielding a gain, is taxable in the year in which the transaction of sale takes place and the gain is made. 7 R. C. L. Sec. 245. Until the shares, whenever purchased, are sold there is neither gain nor loss. A gain springs from a sale and the tax is imposed on the gain in the year of the transaction of sale. That is the "taxable year". Whether or not there is gain or loss in a sale of shares made in the tax year depends on what shares were sold, the last purchased or the first purchased, or shares intermediate the two, which always is a question answered by the taxpayer's evidence, or by the rule, as to the identity of the shares involved.

We find nothing substantial in this defense.

The petitioner's next position is that the "First in, first out" rule, if valid, is inapplicable to the facts of this case. The facts as stated by the petitioner himself are these:

In 1928 and several prior years the petitioning taxpayer dealt, through two brokerage houses in Philadelphia, in stock of the United Gas Improvement Company known to speculators as U. G. I. through marginal accounts by the process known as pyramiding.

[fol. 54] "On January 1, 1928, (the beginning of the tax year) petitioner was long 5300 shares of U. G. I. During the year 1928 the brokers bought for petitioner's account, on his orders, 10,600 additional shares and sold 7,900 shares. On December 31, 1928 (the end of the tax year) petitioner's account was long 8,000 shares, an increase of 2700 shares for the year. All purchases and sales were in the form of 'street certificates' for 100 shares each endorsed in blank by some brokerage house. They (the certificates) were inextricably mingled with other securities pledged with banks. They (the certificates) were at all times incapable of identification as having been bought or sold for account of petitioner."

"All facts alleged are admitted except in regard to petitioner's intention. His intention (to sell the shares last

bought) was proved at the trial by a statement received in lieu of evidence." (The interpolations are ours.) On these facts, and against the action of the Commissioner in charging the shares sold against shares earliest purchased, the petitioner takes the broad position that the rule in question "is inapplicable to sales of shares of stock in the course of operating on margin accounts, because on its face it assumes sales of shares of stock under circumstances which rendered them capable of identification."

In shorter words, his position is that shares of stock sold on margin are incapable of identification, hence the rule does not apply to such transactions.

From the petitioner's statement of facts and his position on the law, it is obvious he has confused identification of shares and identification of certificates in transactions of sale. The rule deals with the sale and identification of "shares of stock in a corporation," not with sale and identification of certificates. Shares of stock and certificates for shares of stock are different legal entities. Shares of stock "are intangible and rest in abstract legal contempla- [fol. 55] tion". They are the interest or right which the owner has in the management, profits and assets of a corporation. 14 C. J. Secs. 506, 509. Though incorporeal, they nevertheless are property and are the subject of conversion. 14 C. J. Sec. 509; 7 R. C. L. Sec. 166; Skinner v. Eaton, Collector, 45 Fed. (2d) 568. A certificate of stock, on the other hand, is the symbol or paper evidence of the ownership of shares; it is not the stock itself. It is merely written evidence, and then only prima facie evidence, of the ownership thereof by the person designated therein and of the rights and liabilities resulting from such ownership. 14 C. J. Secs. 698, 701, 702, 707, 709, 710, 1043. Howbert v. Penrose, 38 Fed. (2d) 577, 579. A stockholder may prove his ownership of shares by evidence other than that of the certificate, 14 C. J. Sec. 1272; and he may dispose of his shares and surrender his title therein by sale accompanied with delivery of a certificate in his name which he has endorsed with a blank assignment and power of attorney authorizing the transfer. 14 C. J. Secs. 1033, 1050; 7 R. C. L. Secs. 239, 243. As between seller and buyer the shares pass by mere delivery of the certificate, so endorsed, though the transfer as between the new owner and the corporation is not complete until made on the books of the corporation. When the

new owner of the shares sells them without first having them transferred to himself on the books of the corporation and makes delivery by handing over the certificate so endorsed in blank by the original holder and starts it on its wanderings through the "street", the shares may go in one direction and the certificate in another; the shares, however, always being represented (in the rapid shifting of certificates between brokers) by a like certificate in the name of another, with endorsement in blank, held for the owner. Then "ownership follows the owner, not the certificate". Howbert v. Penrose, 38 Fed. (2d) 577, 579. While not technically negotiable instruments, certifi- [fol. 56] cates endorsed in blank pass from hand to hand in the "street" and are regarded in a very extensive practice as quasi negotiable. 14 C. J. Secs. 1033, 1041, 1043, 1044. Upon delivery of a certificate in the seller's name endorsed in blank, or upon delivery of a "street certificate" in the name of someone else, similarly endorsed, the contract of sale between buyer and seller (unless burdened with conditions) is complete and the transfer, within taxing statutes, takes place. 7 R. C. L. Sec. 245.

From these observations, abundantly sustained by decisions, it is plain that the petitioner in this case owned shares of U. G. I. stock, though neither he nor his brokers ever held certificates for them in his name; and, owning them, he had power to sell them when he saw fit and make delivery by certificates, issued to other persons, endorsed by them in blank, and held for him by his broker; and when he sold his shares, as he did, he suffered losses or made gains at the time he sold them. Whether or not there were losses or gains, and in what amounts, depends on what shares he sold and the figures at which they were purchased, that is, whether they were the shares he purchased in 1928, the tax year, or were shares he purchased in prior years. Certainly they were one or the other and he was bound to show that factor in the tax calculation by identifying the shares (as by identifying the "lots" in which they were purchased) both for his own protection in paying and for the protection of the government in exacting taxes. In this and perhaps in other ways the "shares" were "capable of identification". All he showed by way of identifying the shares he sold from "lots" previously purchased was his intention always to sell the shares last

purchased. That may be true, yet he did not transmute his intention into action. He did not order his brokers to sell from any particular lot or otherwise give life to his intention. Skinner v. Eaton, Collector, 45 Fed. (2d) 568, [fol. 57] 569; Howbert v. Penrose, 38 Fed, (2d) 577, 578. He proved what he had thought and also proved that he had done nothing about it. If a taxpayer's intention alone were to govern, it would in every instance be conclusive. Being an operation sealed in his mind, it could not be contradicted by anyone outside. Standing alone as in this case, or "in the absence of something else" as we said in the first Snyder case (54 Fed. (2d) 57, 58), the owner's evidence of his bare intention is not sufficient identification of shares he sold to take the case outside the "First in, first out" rule. On this issue we hold, in accord with our decision in Snyder v. Commissioner, 54 Fed. (2d) 57; Horner v. Commissioner, — Fed. (2d) —; and Commissioner v. Merchants and Manufacturers Fire Insurance Company, — Fed. (2d) —, the deficiency tax assessed against the petitioner must be sustained.

Finally, the petitioner represents that aside from the rule we have been discussing, the transactions which were the subject of the tax in question constituted a trade or business which he regularly carried on, within the meaning of Section 22 of the Revenue Act of 1928 permitting (under Section 23 (e) (1)) deductions for losses so incurred. The petitioner averred in his petition for redetermination of the deficiency tax that during a term of years, including the tax year, "in addition to his regular employment as secretary of an insurance company on salary, (he) was engaged in a business regularly carried on for profit which . . . was the purchase and sale of shares of stock listed on" various exchanges. The Commissioner by his answer denied this averment. At the hearing it was stipulated that if the petitioner were present he would testify to its substance. The Commissioner introduced no evidence in contradiction nor did the Board pass upon the matter in its opinion. Taking the record and the evidence as they stand [fol. 58] we must determine whether there was enough shown to compel the finding which the petitioner asks and to call in play the cited statute.

We cannot find on the petitioner's averment and meager evidence that his case falls within the statute. It is clear

that in certain situations a person who has organized a corporation and invested in its stock and has devoted most of his time to its management may be regarded as having regularly carried on the business and be entitled, under the statute, to make appropriate deductions of stock losses from income. Washburn v. Commissioner, 51 Fed. (2d) 949; Schwinn v. Commissioner, 9 B. T. A. 1304. But lacking convincing evidence of a claimed trade or business regularly carried on, it is generally held that deductions of losses incurred in trade in a given tax year are limited to losses incurred in the actual business of the taxpayer as distinguished from isolated transactions, and do not include losses sustained through dealings on an exchange by one engaged in another business. Mente v. Eisner, 266 Fed. 161; Washburn v. Commissioner, 51 Fed. (2d) 949. We must assume from the order under review that, notwithstanding the silence of the Board on the subject, it found. that the petitioner was not engaged in the trade or business he averred. This finding on what may be a mixed question of law and fact is, in our opinion, sustained by the record.

The order of the United States Board of Tax Appeals is affirmed.

A true copy.—Teste:

—— ——, Clerk of the United States Circuit Court of Appeals for the Third Circuit.

[fols. 59 & 60] IN UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD TERM

March Term, 1934

No. 5419

JOHN A. SNYDER, Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE, Respondent

Appeal from the United States Board of Tax Appeals

JUDGMENT—Filed Sept. 18, 1934

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof it is now here ordered, adjudged, and decreed by this Court that the order or decree of the said Board of Tax Appeals in this cause be, and the same is hereby affirmed.

Philadelphia, September 18, 1934.

Victor B. Woolley, Circuit Judge.

[File endorsement omitted.]

[fols. 61-70] Petition for rehearing, covering 10 pages, filed Oct. 18, 1934, omitted from this print. It was denied, and nothing more, by order of Oct. 24, 1934.

[Title omitted]

ORDER DENYING PETITION FOR REHEARING—Filed Oct. 24, 1934

And now, to wit, October 24, 1934, after due consideration, the petition for rehearing in the above-entitled case is hereby denied.

Philadelphia, ——.

Victor B. Woolley, Circuit Judge.

[File endorsement omitted.]

[fol. 72] Clerk's Certificate to foregoing transcript omitted in printing.

[fol. 73] SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed February 4, 1935

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted, and the case is assigned for argument immediately following No. 582.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 39,291. U. S. Circuit Court of Appeals, Third Circuit. Term No. 663. John A. Snyder, Petitioner, vs. Commissioner of Internal Revenue. Petition for a writ of certiorari and exhibit thereto. Filed January 23, 1935. File No. 663, O. T., 1934.

(5973-C)